Joint Committee on Taxation
January 14, 1983
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# SUMMARY OF GAO REPORT TO THE JOINT COMMITTEE ON TAXATION ON IRS'S ADMINISTRATION OF PENALTIES IMPOSED ON TAX RETURN PREPARERS

The U.S. General Accounting Office (GAO) recently issued a report to the Joint Committee on Taxation concerning the IRS' administration of the provisions of the Tax Reform Act of 1976 relating to paid preparers of tax returns ("IRS' Administration of Penalties Imposed on Tax Return Preparers," GAO Report No. GGD-83-6, January 6, 1983). This report was issued in response to a request by the Joint Committee on Taxation. Specifically, the GAO was asked to evaluate whether the provisions of the 1976 Act were (1) helping the IRS to identify returns prepared by paid preparers (disclosure and recordkeeping provisions); (2) deterring preparers from engaging in negligent or fraudulent practices designed to understate taxpayers' tax liabilities (conduct provisions); and (3) deterring preparers from endorsing or negotiating taxpayers' refund checks (conduct provisions).

The following is a brief summary of GAO's findings and conclusions, and recommendations, as well as IRS comments on the report.

## GAO Findings and Conclusions

### Disclosure and Recordkeeping Violations

According to the GAO, the IRS has been successful in getting those return preparers who provide some, but not all, of the identification data required on tax returns to comply more fully with the disclosure requirements of the law. The GAO, however, is concerned that this success may be short lived because of budget constraints.

In contrast, the GAO does not believe the IRS has been as successful in dealing with those return preparers who do not identify themselves on the returns they prepare or who do not keep required records. The GAO has concluded that the IRS needs to gather and analyze data on those preparers in order to determine the extent of the problem and the relative effectiveness of its compliance activities in this regard.

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Conduct Violations

According to the GAO, IRS' administration of conduct-related penalties has been uneven. The GAO has concluded that the IRS should take steps to (1) further improve administration of the penalty for negligent misconduct; (2) clarify the circumstances under which the willful misconduct penalty ought to be asserted; and (3) reevaluate its compliance approach with respect to preparers who endorse or negotiate taxpayers' refund checks.

Program Action Cases

The GAO noted that while the IRS relied primarily on its existing enforcement structure to administer the preparer penalty provisions, it also recognized the need to supplement that approach with a special program aimed at detecting and deterring preparers who consistently violate the law. Through the use of "program action cases," the IRS has sought to assert multiple penalties against preparers who commit multiple violations.

Better Management Information Needed

According to the GAO, the tax return preparer problem is larger than originally anticipated, but the IRS has not sought to identify specifically the size of the problem preparer group. Furthermore, the GAO concluded the the IRS has not collected the data necessary to assess the effectiveness of its administration of the penalty provisions. Specifically, the GAO found that the IRS lacks data on the extent to which penalties have been assessed consistently against the same preparers over the course of several years.

## GAO Recommendations

The GAO concluded that the IRS needs to collect and analyze better management information on the paid preparer population and on preparer penalties. According to the GAO, without this information, the IRS cannot fully assess the extent of preparer noncompliance or the effectiveness of its overall compliance program. In this regard, the GAO suggested that the Commissioner of Internal Revenue may wish to consider using the IRS' Taxpayer Compliance Measurement Program as a means for collecting some of the needed data.

As part of the process of gathering and analyzing management information on the paid preparer noncompliance problem, the GAO recommends that the Commissioner reassess certain IRS compliance approaches and take corrective actions where appropriate. Specifically, the GAO recommends that the Commissioner (1) determine whether a sizeable group of preparers exists who are not identifying themselves on returns they prepare and who have not been detected by IRS' current compliance program; and (2) reevaluate the IRS! current nationwide approach to detecting preparers who negotiate taxpayers' refund checks.

Finally, the GAO made the following recommendations to the Commissioner for the purpose of assuring greater consistency in penalty assertion decisions:

(1) Publish guidelines defining the circumstances under which the willful misconduct penalty ought to be asserted;

(2) Identify additional means through which to better ensure that examiners take tax law complexity into account when making penalty assertion decisions; and

(3) Specify that all penalty case files contain information on the type of penalty assessed, the basis for the penalty action, the dollar amounts involved (especially in terms of understated tax liabilities), and the results of supervisory and quality control reviews.

## IRS Comments

The Commissioner of Internal Revenue generally agreed with the GAO's recommendations and indicated that various corrective actions, along the lines suggested by the GAO, would be initiated. In response to the Commissioner's comments, the GAO suggested further that, in developing corrective actions to the paid preparer program, the IRS should take into account the effect of its plans to reduce taxpayer assistance since such a reduction could have the effect of forcing more taxpayers to seek assistance from paid preparers in the future.

The GAO also commented that the IRS could further assure consistent application of the willful misconduct penalty by seeking to develop guidelines which would better define for IRS personnel and paid preparers the circumstances under which that penalty may be asserted.

## Availability of GAO Report

Additional copies of the GAO report are available from the U.S. General Accounting Office, Document Handling and Information Services Facility, P.O.Box 6015, Gaithersburg, MD 20760; 275-6241.